

**Submission to the
Australian Senate Enquiry**

Into the

TELECOMMUNICATIONS REGIME PRIOR TO T3

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1. INTRODUCTION

The fact that we need yet another Senate Inquiry demonstrates that the current telecommunications regulatory regime is not delivering the outcomes that were envisaged in 1996.

In my submission in relation to the Telecommunications Bill 1996 (now Telecommunications Act 1997) I indicated that it would be impossible to rely on a self-regulatory regime in a market dominated by only one large player. Without a strong regulatory regime it would be impossible to achieve the outcomes envisioned by the government.

Furthermore, I argued that we should take into account in the proposed legislation the likelihood of the emergence of broadband pre-empting the convergence between telecommunications and broadcasting (media).

It is precisely in these two areas that the struggle is now taking place – to make them work for the benefit of all Australians.

Based on numerous reports from the ACCC, PC, ACC, OECD, other Senate Inquiries – and basically everybody else in this country with the exception of Telstra and the government – it is a clear that we have reached the end of the road in relation to the current self-regulatory environment.

Telstra is even more dominant than it was in 1996, making futile every effort by the regulators to stimulate competition and innovation. One of the best examples, of course, is the collapse of the Broadband Competition Notice. This was based on clear evidence that Telstra had breached the country's anti-competitive rules, but, despite this, the regulator was still unable to properly punish Telstra for the offence.

Nor is there any real evidence that the ACCC can prevent such behaviour from happening again.

However, even when operating within perfectly legal boundaries, Telstra is now so powerful that it has become impossible for any competitor to offer serious competition, without obtaining special regulatory support (eg Optus's current requirement in relation to its broadband infrastructure plans).

Of course, this is, economically, a very unhealthy and untenable situation. Such an environment cries out for economic reforms and, if it were not for T3, this government most certainly would have launched such reforms – since economic reform is one of the cornerstones of its overall fiscal policy.

Just as it did in the 1990s, Telstra is persisting with its regulatory game-playing. In the 1990s this was associated with access to the company's voice network. Now it is all about access to data (broadband) networks. Negotiations over the vital local loop unbundling regulations, which are critical for competition in this market, have now been going on for five years – and there is no resolution in sight.

It is not only Telstra's wholesale rates that are hindering competitors from obtaining sustainable margins. Perhaps equally important are the numerous 'conditions' Telstra can use to make life miserable – from access to local exchanges (the key is lost) to uncertainty regarding investment from the competitors. Telstra can change the rules as it wishes – for example, in relation to its future network upgrades (wholesale conditions only apply to copper networks, not to HFC or FttH networks).

Regulators all around the world are facing these problems, and everybody knows very well what the answer is – a range of economic reforms aimed at restructuring the industry.

We have also reached that conclusion in Australia, but, despite numerous investigations, Inquiries, submissions and expert papers, the government is determined not to take the most appropriate action – that is, to seriously explore the possibility of providing the ACCC with divestiture powers.

In the United Kingdom, OFCOM's threat of implementing structural separation, supported by the fact that it actually has the divestiture powers to do so, is currently forcing BT change its behaviour.

Facing the reality of a powerful government that is unwilling to properly address the issue of structural separation, the ACCC should at least be provided with the authority to use this threat as a weapon to force Telstra to change its anti-competitive behaviour and its regulatory game-playing.

Exhibit 1 – Achievable regulatory outcomes

The three key regulatory issues that would be required to move into that direction and which should be achievable within the political reality of the Australian telecoms market today are:

- stronger accounting separation rules, to properly separate wholesale from retail;
- more regulatory powers ; and
- a further strengthening of the government's commitment to the future-proofing of the regional telecoms infrastructure.

I will expand on these, and other, issues later in this report.

2. RECOMMENDATIONS

The main policy issues surrounding the full privatisation of Telstra are:

- generally fostering competition and ensuring that the regulator is an effective enforcer of the competition rules, and
- currently and specifically, ensuring the delivery of broadband services around the country.

Equal access to Telstra's network is not the only important issue – innovation is also crucial for economic growth and social developments. Broadband is the key infrastructure for our knowledge-based society and it has been recognised that it has far-reaching consequences for our economy and our society. It would not be in the national interest for all elements of this section of the economy to be under the control of one player.

Key recommendations to address are:

- Review of the accounting separation rules. The current system should be changed so that the ACCC can set the rules – as distinct from the present situation, where Telstra sets the rules and decides where it draws the line between its retail and wholesale activities. The recommended changes should lead to a much clearer, stable (that is, consistent) and enduring separation between the retail and wholesale divisions, including the separation of systems (billing, accounting, etc). Transparency in Telstra's wholesale pricing to its own retail services would, for the first time, provide the level playing field essential to allow Telstra's competitors to fully participate in telecoms markets in general and the broadband services market in particular. It will also assist in creating a more effective USO policy.
- These accounting separation rules should be strengthened by handing enforceable powers to the ACCC, which would lead to immediate effective action against anti-competitive behaviour. This is essential to prevent the vertically-integrated Telstra from totally dominating many elements of the e-economy. A stable, transparent accounting regime could also reduce the possibility of long-term cross-subsidisation by exposing the excessive economic rents being generated in parts of the value chain.
- Eventually, a clear, stable and enduring accounting separation of wholesale and retail could also possibly allow a move away from retail price caps towards a wholesale price cap model. This would rely on competition to determine retail prices, but would also ensure, in instances where competition is limited and infrastructure is clearly too costly and economically wasteful to duplicate, that wholesale prices be managed to avoid excessive economic rents accruing to the dominant provider.
- A long-term commitment should be made by the government regarding the future-proofing of regional broadband infrastructure. This could be based on a regularly updated USO policy that could be developed, using the current HiBis plan as a starting point. It should include public visibility of area-based aggregate demand registers, USO contracts for roll-out of broadband infrastructure permitting open access to broadband service providers, and the setting of national targets for the percentage of Australian households that need to be connected to broadband by 'milestone' years (see my suggestions below exhibit 2). Bi-annual reviews should monitor progress and finetune the plan as required. The aim is to provide all Australians with equal access to the e-economy and global information sources.

3. REGULATIONS ON HOLD DURING T3

The third tranche of Telstra's privatisation will be one of the largest selldowns ever undertaken – not only in Australia, but internationally – if the government aims to completely exit its holding in Telstra in one selldown.

It will be a massive exercise. The bank syndicate and government will need to be able to generate sufficient interest to attract enough 'mum and dad' investors to subscribe for the bulk of a \$30 billion float and to provide pricing tension against domestic and international investors, including the increasing activity of hedge funds. As in T1 and T2, a substantial part of this investment will probably have to come from retail investors. While many retail investors will make their decision on the current price of Telstra shares at the time of T3 and on fundamentals of the Telstra investment story, many others will need convincing, as they are still reeling from the losses they either have realised, or have yet to realise, from the T2 sale.

Timing will also be a complex issue, which will need to factor in the international equities calendar, budget blackout periods and so on. Furthermore, the need for a full scoping study to determine structure (number of tranches, new sources of demand for Telstra shares, logistics, etc), a change in the Senate, appointment of the banking syndicate, coordination with Telstra's calendar of events, etc, could see late 2005 as a possible date for a further selldown.

The enormity of this exercise will require one of the most serious due diligence projects ever undertaken and it will demand a high degree of certainty around Telstra's position. It is therefore most unlikely that the government, in its capacity as vendor, will wish for any serious regulatory investigation and/or action during, or immediately after, the privatisation project.

This makes it imperative for the government to be satisfied that it has put in place a rigorous, pro-competitive regulatory regime for the industry in advance of any T3 sale.

4. COMPETITION

Competition has lost ground in Australia over the last five years, with fewer competitors operating in the market in 2005 than there were in 1999. But whether there are fewer or more competitors in 2005, the overall profitability of the industry has remained largely the same – 95% of all profits still remains safely in the hands of Telstra.

This is a clear indication that both infrastructure-based competition and services competition have failed to produce sufficient margins for the 1,000 or so new operators (Telcos, ISPs, BSPs) that have to share the other 5% of those profits. Both the infrastructure and services markets are dominated by Telstra, which forces one to question whether the current industry structure will ever be conducive to effective and commercially viable competition.

The ACCC and the PC have indicated that Telstra is currently too large to regulate. Even in the most obvious case of anti-competitive behaviour, when the company lowered its own broadband retail price below its wholesale price, the ACCC has only been able to serve a Competition Notice – it has not been able to halt Telstra's anti-competitive behaviour. This is puzzling the industry and creating enormous anxiety in the market. If the government allows this type of behaviour from Telstra through the lack of proper regulatory protection there is very little hope of any strengthening of competition.

The PC has confirmed that a privatised Telstra will be even more impervious to effective regulation.

After privatisation, Telstra will be under increased pressure from its shareholders to find new growth areas. Its subsidiary, Sensis, has already indicated where it sees its growth coming from – the media industry. It is most likely that Telstra will pursue the acquisition of free-to-air TV stations and newspapers in an effort to bolster its revenues and cross-promote its products. It will then of course become even more powerful in bundling services into cross-media packages for customers, which no other companies will be able to compete with.

Apart from all the anti-competitive aspects of such scenarios, I also would clearly like to flag the likelihood that the ability of Telstra, post-T3, to apply undue lobbying influence across its multiple media assets will undermine the democratic structure of the country and the diversity of the media. It would arguably make Telstra one of the most powerful vertically-integrated telecommunications and media companies in the world. I am not aware of any government in the western world that would allow such a concentration of communication and media power to reside in one company.

Furthermore, new fibre optic access networks could be implemented by Telstra in ways that would make it unprofitable for competitors to access this network. Special regulatory attention, therefore, is needed to prevent this from happening.

5. ARE THE POWERS OF THE ACCC SUFFICIENT

How is it possible that, given the apparently 'blatant' anti-competitive behaviour that has been occurring in the broadband market, the regulator failed to act promptly and decisively. Other issues, such as mobile termination rates, Internet peering and unbundled local loop, demonstrate that the ACCC appears regrettably ineffective.

What more evidence is needed before the ACCC will act. This leads me to conclude that either:

- the ACCC's current powers are insufficient to act or
- the ACCC is not using effectively the powers it had.

The fact that no decisive action is taken plus the fact that the regulator has clearly indicated that Telstra is 'too large to regulate', caused me to conclude that the ACCC indeed is an inadequately empowered regulator.

This was further highlighted by the ACCC apparently indicating that it was having difficulties in obtaining access from Telstra the information that would have given it a good understanding of the wholesale and retail price settings, due to the fact that the wholesale business is currently defined by the carrier under the 'accounting separation' record-keeping regime.

In my opinion it should not be necessary for the ACCC to have the type of 'interview' access to Telstra that the regulator might desire. Simplistically, if a competitor or the ACCC could show that after encouraging a wholesale customer to buy from Telstra, Telstra lowered its retail prices below the wholesale price, there would be a prima facie case that it was designed to 'lessen competition'.

It is also interesting to observe here that, in my discussions with senior management in Telstra's regulatory division, they strongly denied that the regulator doesn't have the power to act, and they maintained that Telstra has provided the regulator with access to senior management in both Telstra's wholesale and retail divisions, which would allow the ACCC to properly investigate those price-setting issues.

Furthermore, Telstra claimed that there is no evidence that it behaved anti-competitively when it lowered its retail prices earlier this year. Its contention is that those who complained about this at the time failed to provide evidence of anti-competitive behaviour. Also, ever since the price changes, Telstra's wholesale broadband providers have maintained their 50%-plus retail market share and so far no one has gone bankrupt – proof, according to Telstra, that its margins are sufficient and that its conduct was not, and is not, anti-competitive.

I think that it would assist everybody involved if this Inquiry clarifies the regulator's position on issues like this. Either the Regulator made a mistake and Telstra was attacked by malicious competitors who wanted a free ride on Telstra's network, or Telstra is 'gaming' the regulatory system and utilising the weaknesses in that system that prevent the ACCC from acting effectively.

I tend to believe the regulator, but I will give Telstra the benefit of the doubt and would like to see some clarity on this issue. Telstra has quite openly provided me with its point of view and a more forthcoming statement of the regulatory position is now needed to resolve the question of what powers are needed by the regulator to effectively and decisively operate, before T3 happens.

6. INDUSTRY APATHY

As I have pointed out before, there is significant industry apathy regarding the upcoming privatisation, with very few companies participating in the debate beyond their own vested interests. It is essential that the industry rouse itself and take part in the national debate in order to establish a viable competitive environment.

The government has a major focus on shareholder issues, and the magnitude of the privatisation has made these even more crucial.

The stakes are very high, and regulatory and competition factors are very low indeed on the agenda of the Prime Minister and the Treasurer. Industry Minister, Nick Minchen, couldn't have been more explicit about not wanting to see any regulations that would lower the T3 share price. In any case, it has become very clear that the government's position on T3 is certainly not geared towards the best interests of the country. The only issue is money – not a better telecoms environment; not more competition; not better services to regional Australia – none of these issues, which are high on the telecommunications agendas of the governments of our trading partners.

If the carrier believed that these were important in the T3 debate it would most certainly have changed its attitude, but there is no indication whatsoever that Telstra, under the pressure of T3, is giving in on any of the issues addressed by the ACCC.

The lack of government and regulatory support has been most discouraging to the industry – to the point where most of the companies no longer endorse the ongoing barrage of Inquiries, which are leading nowhere. This became clear during the ACCC's Inquiry surrounding the Competition Notice.

The burden of these ongoing Inquiries upon companies that are trying to survive on the thinnest of margins is an unrealistic expectation on the part of the ACCC, the Senate and others who are conducting these ongoing investigations within the industry. Despite their undoubted good intentions these Inquiries are getting us nowhere, and this fact has been recognised by the industry.

7. STRUCTURAL SEPARATION

7.1 A TELSTRA-DRIVEN STRUCTURAL SEPARATION?

In an interesting turn of events Telstra's Board voted, on 1 December, to separate its wholesale business into a stand-alone division, in a bid to appease the competition regulator ahead of the company's full privatisation.

The separation would provide greater clarity on the discrepancy in pricing and conditions between what Telstra charges customers through its retail business and what it charges competitors to access its network in its wholesale business.

Of course, it remains to be seen how Telstra will implement this decision. There is no doubt that the ACCC will need to be fully involved in the process, and this Inquiry could be used to provide the ACCC with the appropriate and explicit powers for this.

Structural separation could also ease future political pressure on the government, as there will always be increasing demand for a regulation-driven process as long as Telstra remains a vertically integrated telco, especially when it start moving further into the media industry.

I have been advocating a proper investigation in structural separation since 2001 and it has always been my preferred solution that Telstra should lead this process rather than the regulator.

I am all for an open discussion with Telstra; however the company's track record on industry cooperation is appalling and, since we started with the regulatory debate back in 1992, any of the changes to Telstra's behaviour and its policies that were required under the 1992 and 1997 legislations took place only after lengthy legal battles. Never, ever has a 'cosy' discussion between a Minister and Telstra led to any progress in this field. So the Minister's softly, softly approach will be music to Telstra's ears and will not result in any tangible outcomes. It is up to the Minister to prove that the sceptical and battle-scarred industry is mistaken.

7.2 IS IT FEASIBLE AT THIS STAGE?

The most clear indication that the current regulatory regime is not working is the fact that most observers all agree on the next step, that of economic reforms in the telecoms industry. The current regulatory regime has not delivered the outcome envisaged by the government in 1996. While structural separation might not be a political feasible option before T3, the ACCC should at least be given the powers to break-up the company, even if they won't get used before T3.

What strengthens the regulator's claim that it doesn't have the powers to act decisively, and casts further doubt on Telstra's position as outlined to me by their regulatory management, is the fact that incumbent telcos all around the world have become more formidable, that in many countries competition on the fixed network is faltering, and that regulators are unable to regulate effectively.

The best case study comes from Britain.

7.3 THE BRITISH CASE STUDY

Faced with the technological shift to digital, it became clear to the British regulator, OFCOM, that the current market and regulatory structure was unsustainable.

It is very interesting to note that, in the following sub-chapters, the name BT could quite easily be replaced by Telstra, or, for that matter, by the names of any of the incumbent telco operators in the various western countries

During 2004, OFCOM undertook a Strategic Review of the sector with a view to reassessing the regulatory framework to make it fit-for-purpose against this changing backdrop. During the last few years it had become clear that the limits of the current regulatory framework are concentrated on end-to-end infrastructure competition. Furthermore with the emergence in other markets of service-based competition models, the regulatory framework focused increasingly on the provision of access, at the wholesale level, to BT Group plc's network and facilities.

In November, 2004, OFCOM reported on the second phase of its Strategic Review of the telecommunications sector. This phase takes the form of a follow-up of the consultations and submissions received in response to the first phase, completed in February 2005.

7.4 INCUMBENT REMAINS DOMINANT DESPITE 20 YEARS OF REGULATION

The first phase of the Review, conducted from April to November 2004, identified two principal problems. Firstly, the unstable situation in fixed telecoms – with BT's dominance not offset by a weak and fragmented set of competitors – has led to an insufficiently open and competitive market. Secondly, the sheer scale and complexity of the regulatory framework that has evolved in the effort to liberalise the market, which has attempted, and largely failed, to deliver a desirable outcome through the micro-management of BT's core network.

OFCOM's Review presents three options for discussion in the final phase:

- Firstly, a thorough-going deregulation of the sector, along the lines carried out in New Zealand – with a return to ex-post enforcement of competition law and the retirement of specialist telecommunications regulations.
- Secondly, the regulator could report that the state of the market warranted a full investigation under the provisions of the Enterprise Act – with the potential for a referral to the Competition Commission, and therefore of a restructuring of the market with the break-up of BT.
- Finally, the threat of such a referral could spur BT into a pre-emptive restructuring of its operations and organisation, creating an effective separation between retail service and wholesale network businesses. This is regarded as OFCOM's preferred solution, and BT has indicated its intention to work with the recommendations in the next few months.

7.5 EQUIVALENCE

The paper has been largely welcomed by the industry in the UK, with the notable exception of the ISP community.

The UKIF, an alliance of competitive Internet Service Providers in the UK, has responded with a condemnation of OFCOM's failure to insist on structural separation. Most industry bodies and competitors have stated that the report's mandating of 'equivalent access' to the wholesale network for both competitors' and BT's own retail arms is correct. The long-term result of the change, should it be accepted and acted upon by BT's management, will be to further separate the service provider and wholesale carriage markets – separating services and the carrier technology. In an era of IP-based, converged communications, this seems to be a realistic and workable direction for regulatory policy to take.

7.6 BT REMAINS ON NOTICE

The key question that remains is whether OFCOM's current emphasis on leveraging BT's management into making the radical organisational and structural realignments required to create a genuinely open wholesale business?

Certainly the whole history of BT's response to regulatory directives to date has been one of delay and obfuscation. It does seem likely that the next few months will see a major change in the ex-incumbent's business model. This is partly because, alongside the obvious stick wielded by OFCOM (the threat of

enforced structural separation), the report is carefully padded with various carrots to reward any cooperation given by BT.

The Ofcom "carrot and stick" approach to BT is underpinned by (a) a Comms Act that allows Ofcom to make referrals to the Competition Commission under the Enterprise Act and (b) the existence of divestiture powers in the Enterprise Act.

OFCOM proposes to progressively remove extensive and detailed regulation of various retail telecommunications markets, as soon as it is convinced that an effective competitive market has been created for the end-user. This relies on the rapid achievement of the report's stated aim of 'equivalent access' for BT's competitors in the retail market – and on a massive increase in the levels of transparency and information available for both service providers and customers.

The next few months will be very interesting ones for observers of the British telecommunications market – and, by extension, for all of the evolving telecommunications markets in the developed world. The separation of the retail and wholesale markets, and the similarly expanding divide between content and delivery networks, will require intelligent and forward-looking regulatory structures for the converged electronic communications market.

7.7 OFCOM RECOMMENDATIONS

OFCOM came to the conclusion that structural separation would not be feasible at this time, but it still might be a logical outcome of further reviews in years to come.

A true separation of wholesale and retail, with equal access, is a less disruptive and a more achievable goal.

True, the worry remains that the incumbent – be it BT, Telstra or whoever – will continue to play regulatory games; undermining the process through their armies of lawyers, lobbyists and spin-doctors. Incumbents still control 80%-90% of the fixed networks and there is a high level of scepticism that a more heavy-handed regulatory regime will deliver the required outcomes. However, it seems that this stepped approach will be the way forward, rather than a more disruptive break-up.

More regulatory powers and more regulatory resources are crucial to the new environment. Much more monitoring is required, especially with the massive changes that are going on in IP-based nextgen and Fibre to the Home (FttH) networks. Regulated access to these networks should be provided, linked to a tightening of anti-bundling rules.

As I have already stated above, the regulator (OFCOM, ACCC, etc) needs to be very specific about how it will be able to enforce this process of proper accounting separation or 'equivalence'.

The Minister has indicated that she does like the UK model, but as mentioned above this model is underpinned by very powerful regulations. If the Australian Government continues the self-regulatory regime and refuses to provide the ACCC with divestiture powers there never will be a stick. And all you'll get is more of the same "notional compliance" out of Telstra

8. REGIONAL TELECOMMUNICATIONS

8.1 REINVIGORATE TELSTRA COUNTRY WIDE

There have been significant advances made in Australia regarding regional telecommunications. In the wake of T2, Telstra's Country Wide (TCW) division has certainly made good progress. However, TCW has lost some of its initial gloss and it currently trying hard to reinvigorate its activities to maintain its relevance to regional Australia.

The major problem is that, while this division has an excellent understanding of the regional telecoms needs of the country, it lacks the power to act upon this, since it is primarily a marketing arm and doesn't own the infrastructure. Its influence at a corporate level is limited (and has recently been reduced when the network was split away from Telstra Country Wide).

8.2 HiBis, GOOD EXAMPLE FOR FURTHER DEVELOPMENTS

After my earlier doubts regarding the HiBis scheme I have to say that remarkable progress has been made here also. My criticism of the scheme was, and continues to be, that most of the government subsidies flow back to Telstra, which already makes a \$4 billion annual profit. But, on the positive side, many people in regional Australia are profiting from the new activities and in the satellite area a range of smaller satellite operators are definitely receiving a shot in the arm. There are seven satellite providers participating in the HiBis scheme.

Government policies are aimed at improving broadband in regional Australia, and this is certainly being stimulated by the HiBis scheme. On an international level, this is one of the first government schemes that basically addresses the USO requirements in relation to broadband – and it will be very interesting to see if, under the pressure of T3, this scheme can be turned into a permanent policy.

The government also needs to improve the coordination between the various broadband programs. For example, the program that provides broadband to schools and other government buildings often fails to lead to improved broadband in the wider communities surrounding these facilities. Furthermore, the Demand Aggregation Policy is not delivering the required outcomes and should be urgently reviewed.

8.3 COMPETITION REMAINS FRAGILE

The second important element in regional policies is competition, and this remains a very difficult issue. The short-term demands in regional Australia to obtain broadband are secondary to the need for competition. While it is important to stimulate competition in regional Australia, the reality is that, to a large extent, telecommunications in regional Australia remains a natural monopoly.

That being the case, there certainly needs to be a debate on how better access to Telstra's 'next generation' network can be given to content and services providers in regional Australia. This basically comes back to the competition debate described above, with a proper separation between wholesale and retail.

While extensive information and promotion is rapidly educating metropolitan communities, the same should be happening in regional Australia. Without the commercial push for this the government needs to support programs to bring information regarding the e-economy to businesses and residents in regional communities.

8.4 REGIONAL MOBILE

Mobile is another issue that keeps coming up in regional Australia. As an example, while a lot of attention is given to mobile coverage in remote parts of the country, it was interesting to note that large parts of the Hunter Valley, less than 150Km from Sydney, are still without any mobile coverage.

Telstra, however, has also increased its CDMA coverage in the more remote parts of the country. This has since been upgraded with 1X and EV DO technologies, which have improved data services over the network. While it is not the ideal service for broadband it certainly is a help, especially for business users in regional Australia.

8.5 'UP TO SCRATCH'

Telecommunications services need to be "up to scratch" before the rest of Telstra will be privatised.

If our politicians were serious they should do what their colleagues in other countries have been doing – setting targets.

The National Farmers Federation has indicated that services are 'woefully inadequate' and broadband in regional Australia is 'very limited' (see chapter NFF below). This is in contrast to the conclusions the government draws, they indicate regional telecoms are 'up to scratch'. This Inquiry should shed some measurable light on this issue.

Since the government isn't providing measurable outcomes, I will give you my suggestions:

Exhibit 2 – Future proofing Australia – measurable outcome

By 2006 every Australian household/business should have access to a minimum of 2Mb/s broadband at a price under \$50 per month. By 2010 this should be a minimum of 10Mb/s for the same price, and by 2015 a minimum of 45 Mb/s, again for that price.
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Bi-annual reviews (and certainly not 5-year reviews) should check the validity of these targets and prices, and make adjustments if required. We could also set separate targets – for example, a price of under \$40 for metro services and \$50 for regional services.

It is futile to have the ACA conduct incredibly expensive and complex quarterly calculations in order to gauge the performance of the telcos' old-world services (telephone calls and access). It is utterly futile to continue to measure this – these are the kind of statistics that are needed to evaluate telephone services in developing countries. Australia should have moved on – our 'up to scratch' measurement should reflect our economic and social position in the global marketplace.

That is not to say that we should not keep an eye on the overall quality of the infrastructure, but it should be tested against the performance of new-world services, not against the quality of the old-world services.

8.6 T3 THUMBS DOWN FROM NFF

In December 2004 the National Farmers' Federation indicated it was still too early for the government to sell its remaining stake in Telstra as not enough had been done to protect rural services.

Only around half of the recommendations of the Estens Inquiry into regional telecommunications services had so far been implemented. This regional telecommunications inquiry was completed in 2003 made 36 recommendations, which, if implemented, would provide, broadly, equivalency between rural telecommunications in rural Australia and urban Australia.

By late 2004, only about half of those recommendations have been fully implemented.

The NFF is concerned about this and would like to see that the rest of those recommendations are implemented as soon as possible.

The government has named guarantees on rural services as a pre-condition for completing the sale. They had promised to speed up the necessary improvements, but according to the NFF service and installations times, particularly in remote areas, are woefully inadequate.

The other key issue is broadband, or rather the lack of it, according to the NFF availability in rural Australia is "very limited".

9. INFRASTRUCTURE ISSUES

9.1 CONTRADICTIONARY POLICIES?

There seems to be a certain amount of inconsistency between the government's 'future-proofing' policy and its 'infrastructure competition' policy.

On the one hand, the government is forcing Telstra to enhance its position in regional Australia – even legislating that it retain offices and staff in these areas. On the other, it is talking about encouraging competing infrastructure. There certainly won't be much interest in investing in these areas while Telstra's dominance is basically set in concrete by another set of government regulations.

9.2 INFRASTRUCTURE-BASED COMPETITION

In theory, stimulating competition through complementary infrastructure policies is a great approach, and I would love to be more positive about it. In reality, however, without very strong government support no one will be interested in investing in the current circumstances.

The government would need to indicate precisely which infrastructure it would like to see developed and then offer specific regulatory support to make that happen.

There are a few options that I can see here:

- It could split Foxtel from Telstra and use this network as a base for competition.
- It could sit down with Optus and discuss how their HFC network can be used to offer that level of competition.
- It could use a combination of the above two points.
- It could use the utilities to build competing infrastructure.
- It could offer regional concessions for specific local solutions.

It is also important to note that we are focusing here on what is known as the fixed national network. Mobile networks, of course, do offer competition in certain areas, but they are not a viable alternative to the fixed networks. While there certainly will be further developments in mobile/wireless it is unrealistic to base our future requirements on networks that might, or might not, be able to deliver our national broadband services – or to rely on what these networks are going to be able to deliver. We have seen too much hype from this sector of the industry to base our future national requirements on the wireless technology.

9.3 GOVERNMENT-GUIDED INFRASTRUCTURE UTILITY DEVELOPMENTS

Whatever decision the government takes, it will then have to meet with the companies involved and discuss what regulatory environment they need to achieve the required result. This is not too difficult, as there aren't all that many companies that would be capable of becoming involved in such large-scale, long-term investment plans. The reality of infrastructure-based utility development is that it needs to be a guided process. The open market model we have used for the last ten years has failed dismally.

9.4 NO MORE 'SHE'LL BE RIGHT' POLICIES – PLEASE!

We know all too well what happens if we continue planning using the typical Australian 'she'll be right' attitude.

Here are a few examples:

- Optus started to build competing infrastructure and was 80% overbuilt by Telstra, thus rendering any business model totally useless. The Australian government is the only one in the western world that has allowed this to happen.
- Nextgen, IP 1 and others started to build interstate networks, only to see Telstra drop the wholesale process on their competing infrastructure by 40%-60%. That was the end of competition there. Most of these companies have since gone under.
- A similar story is unfolding in other parts of the country – as soon as a utility has built a competing long-haul network Telstra drops its prices.
- In August 2004 less than 75% of Sydney was covered by ADSL. Unwired entered the market, and within six months Telstra was delivering ADSL to 95% of Sydney.
- A regional operator launched plans to set up a wireless network in Albury/Wodonga and a few weeks later Telstra chose this town to launch the pilot of its own wireless EV-DO alternative.
- This scenario has been repeated in other regional towns. As soon as new initiatives are rolled out by regional telcos Telstra follows with DSL upgrades. Over the last year I have come across at least a dozen such cases. This is extremely disruptive to the policies of state governments and local councils. They allocate funds for broadband upgrades, only to see them undermined by competitive tactics from Telstra.
- Telstra also refuses to work alongside the developers of new estates to deploy FttH based on conditions set by the developers. They simply use their right-of-way to dig a set of trenches next to the alternative FttH infrastructure, once again rendering any serious competition useless.

The Minister does appear to recognise this; however she suggests that a lot of these problems could perhaps be resolved within the current regulatory framework. I find that hard to believe. If the current regime is adequate to protect initiatives such as these, then why have so many of the above projects failed?

9.5 HOW WILL THE MINISTER CONVINCE TELSTRA TO COOPERATE?

The Minister is saying that she doesn't want foolishness like the Optus/Foxtel overbuilding happening again. If she cared to look around she would see that it is continuing on a daily basis. And why wouldn't Telstra do it? It loves its monopolistic position and the government, despite the rhetoric delivered by the Minister, is more than happy to let Telstra get away with it, as any increase in their dominance increases the share price.

These are the realities of infrastructure deployment. No serious competition can happen without regulatory support. If the government is serious about competing infrastructure it had better start looking at protective measurements to make it happen.

9.6 BARKING UP THE WRONG TREE?

But here is the catch. Do we really want this? Is it really necessary?

The Minister herself hinted at the fact that infrastructure deployments often have monopolistic characteristics, it often is a natural monopoly and I certainly agree with her.

Yes, there is infrastructure competition in the USA and Europe, but the foundations for that were laid in the 1960s and 1970s, a totally different era. At the moment the question is: for how long will those HFC cable TV companies be able to compete with the telcos that are rapidly deploying FttH?

If the government wishes to stimulate infrastructure-based competition it will still need to untangle the myriad networks that Telstra owns – all of which are in competition with any new development, whether in Sydney, Hobart, Geelong or Darwin.

9.7 FTTH – THE END OF INFRASTRUCTURE-BASED COMPETITION

With the roll-out of these FttH networks telecommunications traffic and broadcasting traffic can be very efficiently combined over the one network.

FttH is far superior to any other infrastructure, so the economics of it will dictate that more and more services are going to be carried over this one network. It is inconceivable that anybody would want to build competing FttH networks.

True, approximately 20%-25% of customers will fall outside the reach of FttH networks, but, again, whoever the infrastructure provider is in those areas will be the monopolist in whatever technology they use. Here, especially, there is no commercial model that would allow for competing infrastructure.

Now, I would be the first to welcome competition if I could see any ray of hope for it. But I don't want competition for competition's sake, if it is going to point our industry in a direction that would result in financial ruin.

9.8 DUMPING THE RISKS ON STATES AND LOCAL GOVERNMENTS

Reading between the lines, I believe that the Minister is hinting that state and local governments should take the lead. However, the same rules apply here – the Federal Government will have to set up very clear demarcation lines if these governing bodies are to become involved.

But, again, why would we want to do this? We have a first-class infrastructure company – Telstra – and we are legislating to ensure that this company maintains its regional presence, so why not make them fully responsible for all infrastructure – and, yes, by all means force them to utilise the existing infrastructure currently owned by government authorities, local councils and utilities.

9.9 OPEN NETWORKS

Telstra is also very much aware that it will not be able to control all the services that are going to be delivered over true broadband networks (minimum of 10Mb/s), but they will delay any progress here for as long as possible, since that would be in their shareholders' best interests. Eventually, however, it will be to its advantage to open up the infrastructure as much as possible. So structural separation is also in Telstra's interest, and this is something it is aware of – otherwise they wouldn't have made the move in December 2004. With a bit of extra pressure I am sure we can push this development further. The only one not pushing is our stubborn government.

As we speak Telstra is building a Next Generation Network (NGN) that will allow 'level 2' access to the network by services and content providers. Basically this will give the service providers full control over their own services, billing, marketing, management and customer service. So the commercial model for Telstra is moving in that direction, as well as their technology (NGN) model.

So, with a clear vision and policy from the government, they can ask the ACCC and the ACA to develop a regulatory framework to support these technological advances and to make proper network sharing happening.

9.10 HOW TO MAKE PROGRESS IN THE REGIONS?

With that sorted out, the next issue is how to advance the progress of true broadband infrastructure in regional areas, and here, as suggested by the Minister, a sensible sharing approach can be developed.

This needs to be based, in one way or another, on a ring-fencing plan that allows for the development of alternative infrastructure without Telstra breathing down everyone's neck. We also need to consider whether we would want Telstra to be a concession holder as well. I would argue yes, as I still believe they are the best-equipped infrastructure provider.

Caution is also needed, since the regional customers are interested, firstly, in a good set of services, and only secondly in competition. So anybody who is given any sort of concession will need to deliver ironclad outcomes that guarantee the broadbanding of local communities – based on measurable plans, as mentioned above, that need to be developed between these concession holders and the local and state communities.

If the concessions granted are too significant, the concession holders could be tempted to ignore the needs of the local community. In the plans that have been developing with local communities since 2002, I have always been advising the importance of a local steering committees to overlook the broadbanding of their community – with the setting of strong community goals around local social and economic issues. Community issues often become the first casualty of models based on concessions (read ‘monopolies’).

The last thing these communities need is a ‘broadbandaid’.

10. SUMMARY AND CONCLUSION

We have to learn from previous results of regulatory initiatives that while they might have been looking good on paper most have fallen down at the point of implementation. To underpin government policies, and make them a reality, strong, timely and enforceable regulatory strategies need to be put in place.

My preferred outcome would be to follow up on Telstra's announcement regarding its voluntary structural separation and identify where this needs to be supported by enforceable, timely regulatory processes. Twenty years of experience have taught me that without the stick the carrot won't work. I used the British example on the point of separation issues and the big stick that the regulator OFCOM is wielding and the fact that infrastructure-based competition has been in existence here for over 20 years. I haven't seen any big stick from this government; nor have I seen any intention to separate Foxtel from Telstra, which would be the most obvious way to initiate infrastructure-based competition. So how serious is the Minister with her recent announcements regarding infrastructure competition.

Link a serious policy of operational structural separation with a regulatory approach aimed at an open network policy and we would see a good use of the infrastructure on a 'Level 2' basis. Telstra is making commitments towards upgrading to ADSL 2 and FttH, and I believe that, in conjunction with economically feasible wholesale models, this would be by far the best outcome.

And, in areas where this is not going to deliver the required outcomes, let's than look at government-initiated projects around alternative complementary infrastructure, utilising wireless broadband, broadband powerlines (BPL) and satellite-based infrastructure, where it makes sense to do so.

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